

## **Supreme Court interprets VAT exemption for collective asset management in broad terms: management of individual assets via investment profiles is exempt**

On December 4, 2020 the Supreme Court rendered judgments in two important asset management cases. The main question in both cases was whether the VAT exemption for collective asset management can also apply to individual asset management whereby investments are pooled on the basis of investment profiles. Both the Amsterdam and the Arnhem-Leeuwarden Courts of Appeal had ruled in these two cases that the exemption applied. Unlike in the [Opinions](#) issued by Advocate General (hereinafter: AG) Ettema, the Supreme Court confirmed the application of the VAT exemption. The Supreme Court qualified the assets invested in investment profiles as a special investment fund, because the manner in which the assets are pooled and invested is comparable to an undertaking for collective investment in transferable securities (hereinafter: UCITS). The fund is also subject to specific state supervision, because the manager is obliged to have a license and is under the supervision of the Netherlands Authority for the Financial Markets (*Autoriteit Financiële Markten*; hereinafter: AFM).

These judgments will have a major impact on asset managers and their clients, as the Supreme Court has advocated a broader interpretation of the VAT exemption than that of the Deputy Minister of Finance. Asset managers, but also parties that purchase foreign asset management services, must examine whether there is more scope to apply the VAT exemption. If that is the case, then it is advisable to check whether notices of objection can be submitted against the VAT that may have been wrongly paid in the past.

### **1. Background and points of law**

In both cases, the taxpayer is an asset manager that offers an investment product under an individual asset management license. The investment product enables investors to invest their assets in four to five investment profiles, each with a different risk profile. The choice of investment profile depends on the risk an investor is prepared to take. Each investment profile is linked to a model portfolio, which determines the composition of the investment profile. The assets of all the investors within a particular investment profile are invested in the same proportion and in the same financial instruments. Individual deviations from the investment profile are not possible. Aside from the investment and risk profile, investors have no further influence on the choice of investments.

In order to comply with the obligation of the separation of assets arising from the Financial Supervision Act (hereinafter: FSA), investors contribute their assets in a central account of a custodial institution foundation (*stichting bewaarinstelling*) (hereinafter: Foundation). This central account is kept at an external (custodian) bank. The Foundation is the legal beneficiary to the purchased securities and other financial instruments in the central account at the (custodian) bank. The investor has a claim on the Foundation expressed in (fractions of) securities and other financial instruments. The value of the claim is kept via an 'investor giro' account administered by the Foundation. The value of all investments in securities and financial instruments is equal

to the balances of the investor giro accounts. The taxpayers charge the fees for their management services directly to the investors. These are set off against the balance of the individual investment account. In dispute is whether the management services can share in the VAT exemption for the management of special investment funds (hereinafter: collective asset management) pursuant to Section 11(1)(i)(3) VAT Act 1968 (hereinafter: VAT Act).

In her Opinion, the AG had doubts as to whether there were special investment funds. In both cases she proposed that this point be referred back to the relevant Courts of Appeal. With regard to the required specific state supervision, she cautiously concluded that this condition should be met.

The following two points of law were at the heart of both cases:

1. Can the assets of various investors pooled in the bank account of an investor giro or other securities depository, or another pool, suffice to assume that there is a fund?
2. Can the requirement that the managed assets are under specific state supervision also be met if the manager provides its services under an individual asset management license?

## **2. Supreme Court judgment**

In one of the two cases, the Supreme Court substantiated its judgment. It did not do so in the other case. In both cases though the Supreme Court ruled in the taxpayer's favor.

With regard to the first point of law, the Supreme Court confirmed that the assets held in investor giro accounts qualify as a fund that is comparable with a UCITS. According to the Supreme Court, there is a fund if:

1. the assets of various investors are pooled and invested across various financial instruments;
2. by the pooling the investor risk is spread; and
3. each investor has a proportionate stake in the investments but does not own the investments itself.

In these cases, the assets were not pooled in exchange for the issue of shares or units of participation. The investors have a claim on the Foundation in proportion to the assets they have invested. According to the Supreme Court, this difference is, in principle, irrelevant. The Supreme Court has taken a decision in principle and considers it decisive that the participants are entitled to the (monetary) value of a proportionate part of the assets of the fund.

Another aspect of these cases was that the asset managers that raised the money from the investors do not invest the assets themselves but leave this to the Foundation. According to the Supreme Court, this does not alter the comparability with

a UCITS. On this point, the Supreme Court followed the ruling of the Court of Appeal that after investors contribute their assets, they no longer have any control over the purchase and sale of financial instruments.

According to the AG, in order to be comparable to a UCITS, a fund must have a certain de facto corporate independence and, moreover, qualify as a VAT taxable person. The Supreme Court did not stipulate these requirements.

The second point of law related to the requirement of specific state supervision. It follows from the judgment by the Court of Justice of the European Union in the *Fiscale Eenheid X* case, that a fund is comparable with a UCITS if it is under specific state supervision that is comparable with the supervision applying to (the managers of) a UCITS. The Deputy Minister of Finance has taken the position that the taxpayer's individual asset management license is not sufficiently comparable.

However, the Supreme Court ruled that the requirement of specific state supervision had been met. It thus followed the ruling by the Court of Appeal that a license for collective asset management broadly imposes requirements on an asset manager that are comparable to those imposed under a license for individual asset management, and that the differences are only in the detail. The Supreme Court added that the licensing obligation system contained in the FSA and the supervision by the AFM can be regarded as specific state supervision. According to the Supreme Court, the assets of a fund, not being a UCITS, are under specific state supervision if the manager has an FSA-regulated license and thus is subject to supervision by the AFM. For the requirement of specific state supervision, it is therefore not necessary that the supervision focuses on the assets, as the Deputy Minister argues. It is sufficient that the manager or the fund is under the supervision of the AFM.

### **3. Impact on Dutch practice**

The judgments by the Supreme Court will have a major impact on asset managers and their clients. In particular, the Supreme Court's elaboration of the 'fund' concept and the required specific state supervision will have implications for the scope of the VAT exemption for collective asset management.

With regard to the fund concept, the Supreme Court has taken a fundamental decision. To qualify as a special investment fund, it is not necessary that shares or other units of participation are issued. It is sufficient that the participants are entitled to the (monetary) value of a proportionate part of the assets of the fund. This right does not have to be a right to the equity of the fund. The Supreme Court referred here to the ATP judgment of the Court of Justice of the European Union, which shows that a pension fund in which participants also have no shares or units of participation may, under certain conditions, qualify as a special investment fund. The cases on which the Supreme Court has now rendered judgment concern a claim on the Foundation, which does not constitute a participation in the equity of the Foundation. The judgment by the Supreme Court means that many more funds and pooled investments can be regarded

as special investment funds within the meaning of the VAT exemption for collective asset management. This applies to situations involving investor giro accounts, but also for example to CLO, CBO, CDO and CSO companies that pool assets by issuing various classes of loans, derivatives, securities and other debt instruments. Such funds and companies may qualify as a special investment fund insofar as the participants are entitled to the (monetary) value of a proportionate part of the assets of the fund. This is in any case also important in the context of the [defined position on CLO, CBO, CDO and CSO companies, which the Dutch tax authorities recently canceled](#).

In addition, it is noteworthy that the Supreme Court formulated the investor risk test somewhat differently than in the ATP judgment and in its judgment of December 9, 2016 concerning a defined benefit pension fund. For the Supreme Court it is sufficient that a participant is entitled to a proportionate share of the assets of the fund. This may create more scope to regard pension funds as special investment funds and thus to regard their management as VAT-exempt.

The Supreme Court also advocates a broader interpretation of the concept of 'specific state supervision'. Since the Fiscale Eenheid X judgment by the Court of Justice of the European Union it has been clear that funds are only comparable with a UCITS if they are under specific state supervision. For a long time, it was unclear what supervision qualified as specific state supervision. The Deputy Minister of Finance has elaborated on this criterion in the [Specific State Supervision Decree](#). According to the Supreme Court, it is sufficient if the manager of a fund is under the supervision of the AFM, whereby it is irrelevant whether this supervision results from a license for collective asset management or a license for individual asset management. This elaboration of the criterion of specific state supervision is broader than in the Decree. Contrary to the Deputy Minister's view, cases in which this requirement could be met concern exempt investment funds (*vrijgestelde beleggingsinstellingen*; VBIs), mutual funds (*fondsen voor gemene rekening*; FGRs) of which the manager does not fall under the license or registration obligation of the AIFM Directive, and pooling of assets by pension funds, but also CLO, CBO, CDO and CSO companies.

The judgment by the Supreme Court relates to managers subject to a licensing obligation that are established in the Netherlands and are under the supervision of the AFM. The question is when do foreign asset managers of Dutch funds that are obliged to have a license qualify for the requirement of specific state supervision. It seems reasonable to us that if the foreign supervisory regime imposes requirements that are generally comparable with the Dutch supervisory regime – also if that is a regime for individual asset management – this supervision qualifies as specific state supervision. Besides, with its elaboration of specific state supervision and the fund concept, the Supreme Court does appear to be deviating from the way in which other Member States deal with the interpretation of the VAT exemption for collective asset management.

The Supreme Court's elaboration of the requirement of specific state supervision means that the Specific State Supervision Decree will in any case have to be amended to a significant extent.

#### **4. Your options**

The ruling by the Supreme Court is extremely important for the entire asset management market. It is particularly important that asset managers examine whether for various clients there is indeed a special investment fund. There may be more scope to apply the VAT exemption for collective asset management, which may be to the client's advantage. In addition, the ruling by the Supreme Court is important for parties that purchase asset management services from abroad on which they currently report and pay reverse-charged VAT, that is not or hardly recoverable.

It is important to determine as quickly as possible whether there is scope to apply the VAT exemption for collective asset management. If that is the case, then we recommend that, where possible, you submit a notice of objection against the payment of VAT soon. The deadline for submitting notices of objection may still not have expired for VAT that was paid in the VAT return for the third quarter of 2020 or, if you file monthly VAT returns, for September and October 2020.

If you would like to discuss these judgments, feel free to contact the advisors of Meijburg & Co's Indirect Tax Financial Services Group or your usual tax advisor.

Meijburg & Co  
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